

AUDIT DIVISION STATISTICAL SUMMARY

(See also Exhibits in back of Report.)

The following information is based on 100% of the audits completed, taxpayers assisted and special projects conducted during Fiscal Year 1999, and addresses the requirements set forth by IC 6-8.1-14-4(2). Standard Industrial Codes are used to report statistics for the various industries. See Page 40 for an Index of exhibits and charts listed.

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Taxpayers Served In District Offices

Taxpayer assistance is available in all district offices. Each office has a Taxpayer Assistance Supervisor and Assistant Taxpayer Assistance Supervisor who perform taxpayer service functions, as well as other office support responsibilities. Some offices have a field investigator who supports taxpayer assistance. Field investigators also perform collection functions in their districts. Contract employees are available throughout the year to support taxpayer assistance.

The "Taxpayer Assistance Report" (Exhibit A) includes the number of taxpayers assisted (in person and by telephone) and the amount of money collected and assessed by each office. Exhibit A reveals that during

Fiscal Year 99, District Offices assisted 219,484 taxpayers in person and 360,084 taxpayers through telephone contact. Total taxpayers served by the District Offices was 579,568.

The district office in Merrillville served 31,185 taxpayers in person, the highest number of any district office. The Kokomo District Office served 30,761 taxpayers in person, the second highest total.

The Merrillville District Office served 62,490 taxpayers by telephone, while the Bloomington District Office served 49,964 taxpayers by telephone. These were the highest number of telephone contacts among the district offices, representing 17% and 14%, respectively. The Merrillville District Office served a total of 93,675

taxpayers by telephone and walk-in assistance while Kokomo served 61,946 taxpayers by telephone and walk-in assistance.

"Taxpayer Assistance/Special Project Statistics" (Exhibit B) provides the number of hours devoted by field auditors in the District Offices to assist taxpayers and conduct special projects. This exhibit reveals that 15,879 auditor hours were channeled in this direction.

Special Projects

One special project pursued by the Audit Division during the 1999 Fiscal Year deserves mention: Project Comply 99. The Comply 99 project is summarized below.

Project Comply 99

This project commenced at the conclusion of Project Comply IV and was conducted statewide. These audits identified candidates who were usually small and would normally not meet the criteria for a regular audit examination. The results of Project Comply 99 are:

Audits Completed	1,279
Average Hours Per Audit	17.93
Assessments	\$1,067,047
Refunds	\$ 169,214

Gross Income Tax Violations

The most frequently violated gross income tax rule was 45 IAC 1-1-96. This rule defines gross receipts from services. Such receipts include all amounts charged for labor and expenses that form an integral part of the completion of the contract. Statistics show 85 violations of this rule, or 17.42% of all violations of the gross income tax rules. This was also the most frequently violated rule in the previous three studies, accounting for 12.03% of violations in FY98, 12.26% in FY97 and 12.07% in FY96, respectively.

The second most frequently violated gross income tax rule was 45 IAC 1-1-8. This rule defines receipts as the entire gross income or gross receipts derived from all sources and which are actually or constructively received by a taxpayer, credited to the taxpayer or paid to a creditor by another party. There were 35 violations of 45 IAC 1-1-8, or 7.17% of gross income tax rule violations. This rule ranked third in the FY98 study (6.39%) and second in the FY97 study (6.69%).

Ranking third, and accounting for 29 or 5.94% of the gross income tax rule violations, was Rule 45 IAC 1-1-213. This rule requires withholding from any and all

payments made to a nonresident contractor for performance of any work or services taxable to the State of Indiana. This rule also ranked as the third most violated rule in the 1992 study with a 6.55% rate of error. The 1998 study revealed the third ranked rule to be 45 IAC 1-1-8 with an error rate of 6.39%. In the 1997 study, Rule 45 IAC 1-1-120 ranked third with a 5.65% error rate.

Sales/Use Tax Violations

The current fiscal year and previous statistical studies reveal the three most violated sales and use tax rules are the same for fiscal years 1999, 1998 and 1997. The rules are shown below with their percentage of total violations for the three years.

Most frequently violated:	45 IAC 2.2-3-4 ¹		
	<u>1999</u>	<u>1998</u>	<u>1997</u>
	15.64%	16.52%	18.87%

Second most frequently violated:	45 IAC 2.2-3-20 ²		
	14.62%	12.55%	11.61%

Third most frequently violated:	45 IAC 2.2-5-8 ³		
	9.48%	10.20%	10.71%

¹Rule 45 IAC 2.2-3-4 imposes use tax on "tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana . . . unless the Indiana state gross retail tax (sales tax) has been collected at the point of purchase." This rule was violated 658 time in FY99, 687 times during FY98, as opposed to 775 times for FY97.

²Rule 45 IAC 2.2-3-20 states that if the seller of tangible personal property for storage, use, or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit use tax directly to the Department. This rule accounted for 615 violations in FY99, 522 violations in FY98, while 477 violations occurred in FY97.

³The third most violated Sales and Use Tax rule was 45 IAC 2.2-5-8. This rule clarifies the sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools, and equipment used in direct production and other activities. The failure of taxpayers to comply with this rule accounted for 399 of FY99 violations and 424 of FY98 violations. This rule accounted for 440 violations during FY97.

Corporate Adjusted Gross Income Tax Violations

Corporate taxpayers violated adjusted gross income Rule 45 IAC 3.1-1-97 more than any other rule. This rule addresses the returns and reports that must be filed by adjusted gross income tax withholding agents. Violations (282) of this rule accounted for 21.78% of the total violations. This was also the most violated rule in the FY98 study, accounting for 20.92% of the total violations while FY97 study revealed 22.14% of the violations.

Rule 45 IAC 3.1-1-8 was the second most frequently violated rule under this study. This rule states that "taxable income" as defined in the Internal Revenue Code is modified in several ways to arrive at Indiana adjusted gross income. These violations (199) account for 15.37% of the total violations in FY99. The FY98 review showed a 16.58% violation rate while FY97 violations represented a 17.35% rate.

The third most frequently violated rule is 45 IAC 3.1-1-9. This rule deals with the adoption of modifications as defined in the Internal Revenue Code. More specifically, it allows a net operating loss as a deduction in computing Indiana Adjusted Gross Income (IRS Code Section 172). This rule accounts for 106, or 8.19% of the violations of adjusted gross income tax rules. In FY98 and FY97 violations for this rule also ranked third with 7.07% and 7.96%, respectively.

Amounts of Tax Assessed

Exhibits C, D and E display the amount of assessments (refunds) and violations of the gross income tax, sales tax and adjusted gross income tax administrative rules, respectively. "Total assessments" for any tax type represent gross assessments, less amounts refunded.

The amount assessed for each of the most frequent violations and the percentage of the amount to total assessments are presented below:

Gross Income Tax—Exhibit C:

Violation	Amount Assessed	% of All Assessments
45 IAC 1-1-96	\$1,628,420	25.00%
45 IAC 1-1-8	\$ 701,191	10.77%
45 IAC 1-1-213	\$ 397,017	6.10%

Sales/Use Tax—Exhibit D:

Violation	Amount Assessed	% of All Assessments
45 IAC 2.2-3-4	\$5,172,698	18.89%
45 IAC 2.2-3-20	\$2,775,981	10.14%
45 IAC 2.2-5-8	\$6,358,699	23.23%

Corporate Adjusted Gross Income Tax—Exhibit E:

Violation	Amount Assessed	% of All Assessments
45 IAC 3.1-1-97	\$ 865,133	3.54%
45 IAC 3.1-1-8	\$4,811,734	19.70%
45 IAC 3.1-1-9	\$5,860,248	23.99%

Industry/Business Most Frequently in Violation

For the seventh consecutive fiscal year, the most violations of the gross income tax rules were made by taxpayers engaged in manufacturing. This group committed 182 violations or 37.30% of the total violations. The gross income tax rule most frequently violated by this group of taxpayers was 45 IAC 1-1-96. This rule defines gross receipts from services.

The second largest number of gross income tax violations was committed by taxpayers in the service industry. This group committed 117 infractions, or 23.98% of the total violations. The service industry ranked second in the FY95 study. Wholesalers and retailers were the second most frequent violators of these rules in the FY94, FY96, FY97 and FY98 studies. Rule 45 IAC 1-1-120 was most frequently violated by this group of taxpayers during Fiscal Years 1998 and 1997. The most frequently violated rule in the FY95 study was 45 IAC 1-1-96.

As in the previous eight years, wholesalers and retailers were the most frequent violators of the sales and use tax rules. The statistics indicate 1,297 violations, or 30.83% of the total sales and use tax violations. The rule most frequently violated by these taxpayers was 45 IAC 2.2-3-20. As previously noted, this was the second most violated sales and use tax rule in the study by all taxpayers.

Continuing the correlation to the previous eight years, manufacturers were the second most frequent violators of the sales and use tax rules. There were 1,213 violations committed by this group, representing 28.83% of the total violations. The rule most frequently violated by manufacturers was 45 IAC 2.2-5-8, which clarifies

the sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools, and equipment used in direct production and other activities.

With 589 infractions, manufacturers were the most frequent violators of adjusted gross income tax rules. This figure represents 45.48% of the total adjusted gross income tax violations for FY99.

Wholesalers and retailers were the second most frequent violators of the adjusted gross income tax rules. These two groups committed 255 infractions, or 19.69% of the adjusted gross income tax violations.

The most violated rule by manufacturers was 45 IAC 3.1-1-8, which deals with IRS Code modifications to arrive at Indiana adjusted gross income. The rule most violated by the wholesalers and retailers was 45 IAC 3.1-1-97, which addresses returns and reports filed by adjusted gross income tax withholding agents.

Special Tax Violations

Exhibit F provides the number of special tax rule violations and the amount of special tax assessments and refunds.

Article VII of the International Fuel Tax Agreement (IFTA) was the most frequently violated special tax item in the study. It specifies that jurisdictions may require payment of motor fuels taxes on retail sales of motor fuels delivered into fuel tanks that propel motor vehicles. Article VII was violated 209 times and yielded \$51,038 in refunds for the State of Indiana. This represents 28.75% of total violations.

The exhibit also reveals that Article III of the International Fuel Tax Agreement (IFTA) was the second most frequently violated section of the special tax statutes. This section specifies that the taxable event is the consumption of motor fuel in the propulsion of qualified motor vehicles, except fuel consumed that is exempt from taxation by a jurisdiction. All acquired motor fuel that is normally subject to consumption tax is taxable unless proof to the contrary is provided by the licensee. This section was violated 199 times, accounting for 27.37% of the total violations. These violations resulted in assessments of \$470,878.

Miscellaneous Taxes and Penalties

Exhibit G provides the number of violations and assessment amounts of the following:

Financial Institutions Tax
Penalty and Interest Assessments
Food and Beverage Tax
Innkeeper's Tax

A review of this exhibit reveals that IC 6-8.1-4-2 was violated 31 times. This code section addresses access to accounting records of a business and the use of sampling techniques for auditing purposes. These violations yielded \$156,362 in net assessments.

The 18 violations of 45 IAC 15-9-2 yielded a total of \$502,745 in assessments. This section defines the statute of limitations as it applies to refunds.

Number of Years in the Audit Period

The audit period was three years.

Use of Professional Tax Preparation Assistance

The services of professional preparers were used in the preparation of 75.50% of the corporate income tax returns and 11% of the sales tax returns. These findings remain consistent with the previous years' reports.

Filing of Appropriate Tax Returns

A review of Audit Division statistics for various filing statutes of Gross Income Tax, Adjusted Gross Income Tax, Sales and Use Tax, Special Tax and miscellaneous taxes shows 329 violations, resulting in \$768,310 in refunds and \$1,647,559 in assessments. Taxpayers in violation of these rules failed to file the correct tax returns.